

direct that any amount held by the insurer under the contract at her death shall be paid to her estate.

§ 20.2056(b)-7 Election with respect to life estate for surviving spouse.

(a) *In general.* Subject to section 2056(d), a marital deduction is allowed under section 2056(b)(7) with respect to estates of decedents dying after December 31, 1981, for qualified terminable interest property as defined in paragraph (b) of this section. All of the property for which a deduction is allowed under this paragraph (a) is treated as passing to the surviving spouse (for purposes of § 20.2056(a)-1), and no part of the property is treated as passing to any person other than the surviving spouse (for purposes of § 20.2056(b)-1).

(b) *Qualified terminable interest property—(1) In general.* Section 2056(b)(7)(B)(i) provides the definition of *qualified terminable interest property*.

(i) Terminable interests described in section 2056(b)(1)(C) cannot qualify as qualified terminable interest property. Thus, if the decedent directs the executor to purchase a terminable interest with estate assets, the terminable interest acquired will not qualify as qualified terminable interest property.

(ii) For purposes of section 2056(b)(7)(B)(i), the term *property* generally means the *entire interest in property* (within the meaning of § 20.2056(b)-5(d)) or a *specific portion of the entire interest* (within the meaning of § 20.2056(b)-5(c)).

(2) *Property for which an election may be made—(i) In general.* The election may relate to all or any part of property that meets the requirements of section 2056(b)(7)(B)(i), provided that any partial election must be made with respect to a fractional or percentage share of the property so that the elective portion reflects its proportionate share of the increase or decrease in value of the entire property for purposes of applying sections 2044 or 2519. The fraction or percentage may be defined by formula.

(ii) *Division of trusts—(A) In general.* A trust may be divided into separate trusts to reflect a partial election that has been made, or is to be made, if authorized under the governing instru-

ment or otherwise permissible under local law. Any such division must be accomplished no later than the end of the period of estate administration. If, at the time of the filing of the estate tax return, the trust has not yet been divided, the intent to divide the trust must be unequivocally signified on the estate tax return.

(B) *Manner of dividing and funding trust.* The division of the trust must be done on a fractional or percentage basis to reflect the partial election. However, the separate trusts do not have to be funded with a pro rata portion of each asset held by the undivided trust.

(C) *Local law.* A trust may be divided only if the fiduciary is required, either by applicable local law or by the express or implied provisions of the governing instrument, to divide the trust on the basis of the fair market value of the assets of the trust at the time of the division.

(3) *Persons permitted to make the election.* The election referred to in section 2056(b)(7)(B)(i)(III) must be made by the executor that is appointed, qualified, and acting within the United States, within the meaning of section 2203, regardless of whether the property with respect to which the election is to be made is in the executor's possession. If there is no executor appointed, qualified, and acting within the United States, the election may be made by any person with respect to property in the actual or constructive possession of that person and may also be made by that person with respect to other property not in the actual or constructive possession of that person if the person in actual or constructive possession of such other property does not make the election. For example, in the absence of an appointed executor, the trustee of an intervivos trust (that is included in the gross estate of the decedent) can make the election.

(4) *Manner and time of making the election—(i) In general.* The election referred to in section 2056(b)(7)(B)(i)(III) and (v) is made on the return of tax imposed by section 2001 (or section 2101). For purposes of this paragraph, the term *return of tax imposed by section 2001* means the last estate tax return filed by the executor on or before the

due date of the return, including extensions or, if a timely return is not filed, the first estate tax return filed by the executor after the due date.

(ii) *Election irrevocable.* The election, once made, is irrevocable, provided that an election may be revoked or modified on a subsequent return filed on or before the due date of the return, including extensions actually granted. If an executor appointed under local law has made an election on the return of tax imposed by section 2001 (or section 2101) with respect to one or more properties, no subsequent election may be made with respect to other properties included in the gross estate after the return of tax imposed by section 2001 is filed. An election under section 2056(b)(7)(B)(v) is separate from any elections made under section 2056A(a)(3).

(c) *Protective elections*—(1) *In general.* A protective election may be made to treat property as qualified terminable interest property only if, at the time the federal estate tax return is filed, the executor of the decedent's estate reasonably believes that there is a bona fide issue that concerns whether an asset is includible in the decedent's gross estate, or the amount or nature of the property the surviving spouse is entitled to receive, i.e., whether property that is includible is eligible for the qualified terminable interest property election. The protective election must identify either the specific asset, group of assets, or trust to which the election applies and the specific basis for the protective election.

(2) *Protective election irrevocable.* The protective election, once made on the return of tax imposed by section 2001, cannot be revoked. For example, if a protective election is made on the basis that a bona fide question exists regarding the inclusion of a trust corpus in the gross estate and it is later determined that the trust corpus is so includible, the protective election becomes effective with respect to the trust corpus and cannot thereafter be revoked.

(d) *Qualifying income interest for life*—(1) *In general.* Section 2056(b)(7)(B)(ii) provides the definition of *qualifying income interest for life*. For purposes of section 2056(b)(7)(B)(ii)(II), the sur-

living spouse is included within the prohibited class of powerholders referred to therein. A power under applicable local law that permits the trustee to adjust between income and principal to fulfill the trustee's duty of impartiality between the income and remainder beneficiaries that meets the requirements of §1.643(b)-1 of this chapter will not be considered a power to appoint trust property to a person other than the surviving spouse.

(2) *Entitled for life to all income.* The principles of §20.2056(b)-5(f), relating to whether the spouse is entitled for life to all of the income from the entire interest, or a specific portion of the entire interest, apply in determining whether the surviving spouse is entitled for life to all of the income from the property regardless of whether the interest passing to the spouse is in trust.

(3) *Contingent income interests.* (i) An income interest for a term of years, or a life estate subject to termination upon the occurrence of a specified event (e.g., remarriage), is not a qualifying income interest for life. However, a qualifying income interest for life that is contingent upon the executor's election under section 2056(b)(7)(B)(v) will not fail to be a qualifying income interest for life because of such contingency or because the portion of the property for which the election is not made passes to or for the benefit of persons other than the surviving spouse. This paragraph (d)(3)(i) applies with respect to estates of decedents whose estate tax returns are due after February 18, 1997. This paragraph (d)(3)(i) also applies to estates of decedents whose estate tax returns were due on or before February 18, 1997, that meet the requirements of paragraph (d)(3)(ii) of this section.

(ii) Estates of decedents whose estate tax returns were due on or before February 18, 1997, that did not make the election under section 2056(b)(7)(B)(v) because the surviving spouse's income interest in the property was contingent upon the election or because the non-elected portion of the property was to pass to a beneficiary other than the surviving spouse are granted an extension of time to make the QTIP election

if the following requirements are satisfied:

(A) The period of limitations on filing a claim for credit or refund under section 6511(a) has not expired.

(B) A claim for credit or refund is filed on Form 843 with a revised Recapitulation and Schedule M, Form 706 (or 706NA) that signifies the QTIP election. Reference to this section should be made on the Form 843.

(C) The following statement is included with the Form 843: "The undersigned certifies that the property with respect to which the QTIP election is being made will be included in the gross estate of the surviving spouse as provided in section 2044 of the Internal Revenue Code, in determining the federal estate tax liability on the spouse's death." The statement must be signed, under penalties of perjury, by the surviving spouse, the surviving spouse's legal representative (if the surviving spouse is legally incompetent), or the surviving spouse's executor (if the surviving spouse is deceased).

(4) *Income between last distribution date and date of spouse's death.* An income interest does not fail to constitute a qualifying income interest for life solely because income between the last distribution date and the date of the surviving spouse's death is not required to be distributed to the surviving spouse or to the estate of the surviving spouse. See § 20.2044-1 relating to the inclusion of such undistributed income in the gross estate of the surviving spouse.

(5) *Pooled income funds.* An income interest in a pooled income fund described in section 642(c)(5) constitutes a qualifying income interest for life for purposes of section 2056(b)(7)(B)(ii).

(6) *Power to distribute principal to spouse.* An income interest in a trust will not fail to constitute a qualifying income interest for life solely because the trustee has a power to distribute principal to or for the benefit of the surviving spouse. The fact that property distributed to a surviving spouse may be transferred by the spouse to another person does not result in a failure to satisfy the requirement of section 2056(b)(7)(B)(ii)(II). However, if the surviving spouse is legally bound to transfer the distributed property to an-

other person without full and adequate consideration in money or money's worth, the requirement of section 2056(b)(7)(B)(ii)(II) is not satisfied.

(e) *Annuities payable from trusts in the case of estates of decedents dying on or before October 24, 1992, and certain decedents dying after October 24, 1992, with wills or revocable trusts executed on or prior to that date—(1) In general.* In the case of estates of decedents within the purview of the effective date and transitional rules contained in § 20.2056(b)-7(e)(5), a surviving spouse's lifetime annuity interest payable from a trust or other group of assets passing from the decedent is treated as a qualifying income interest for life for purposes of section 2056(b)(7)(B)(ii).

(2) *Deductible interest.* The deductible interest, for purposes of § 20.2056(a)-2(b), is the specific portion of the property that, assuming the applicable interest rate for valuing annuities, would produce income equal to the minimum amount payable annually to the surviving spouse. If, based on the applicable interest rate, the entire property from which the annuity may be satisfied is insufficient to produce income equal to the minimum annual payment, the value of the deductible interest is the entire value of the property. The value of the deductible interest may not exceed the value of the property from which the annuity is payable. If the annual payment may increase, the increased amount is not taken into account in valuing the deductible interest.

(3) *Distributions permissible only to surviving spouse.* An annuity interest is not treated as a qualifying income interest for life for purposes of section 2056(b)(7)(B)(ii) if any person other than the surviving spouse may receive, during the surviving spouse's lifetime, any distribution of the property or its income (including any distribution under an annuity contract) from which the annuity is payable.

(4) *Applicable interest rate.* To determine the applicable interest rate for valuing annuities, see sections 2031 and 7520 and the regulations under those sections.

(5) *Effective dates.* (i) The rules contained in § 20.2056(b)-7(e) apply with respect to estates of decedents dying on or before October 24, 1992.

(ii) The rules contained in § 20.2056(b)-7(e) apply in the case of decedents dying after October 24, 1992, if property passes to the spouse pursuant to a will or revocable trust executed on or before October 24, 1992, and either—

(A) On that date, the decedent was under a mental disability to change the disposition of his property and did not regain his competence to dispose of such property before the date of death; or

(B) The decedent dies prior to October 24, 1995.

(iii) Notwithstanding the foregoing, the rules contained in § 20.2056(b)-7(e) do not apply if the will or revocable trust is amended after October 24, 1992, in any respect that increases the amount of the transfer qualifying for the marital deduction or alters the terms by which the interest so passes to the surviving spouse.

(f) *Joint and survivor annuities.* [Reserved]

(g) *Application of local law.* The provisions of local law are taken into account in determining whether the conditions of section 2056(b)(7)(B)(ii)(I) are satisfied. For example, silence of a trust instrument as to the frequency of payment is not regarded as a failure to satisfy the requirement that the income must be payable to the surviving spouse annually or more frequently unless applicable local law permits payments less frequently.

(h) *Examples.* The following examples illustrate the application of paragraphs (a) through (g) of this section. In each example, it is assumed that the decedent, D, was survived by S, D's spouse and that, unless stated otherwise, S is not the trustee of any trust established for S's benefit.

Example 1. Life estate in residence. D owned a personal residence valued at \$250,000 for estate tax purposes. Under D's will, the exclusive and unrestricted right to use the residence (including the right to continue to occupy the property as a personal residence or to rent the property and receive the income) passes to S for life. At S's death, the property passes to D's children. Under applicable local law, S must consent to any sale of the property. If the executor elects to

treat all of the personal residence as qualified terminable interest property, the deductible interest is \$250,000, the value of the residence for estate tax purposes.

Example 2. Power to make property productive. D's will established a trust funded with property valued for estate tax purposes at \$500,000. The assets include both income producing assets and non-productive assets. S was given the power, exercisable annually, to require distribution of all of the trust income to herself. No trust property may be distributed during S's lifetime to any person other than S. Applicable local law permits S to require that the trustee either make the trust property productive or sell the property and reinvest in productive property within a reasonable time after D's death. If the executor elects to treat all of the trust as qualified terminable interest property, the deductible interest is \$500,000. If the executor elects to treat only 20 percent of the trust as qualified terminable interest property, the deductible interest is \$100,000, i.e., 20 percent of \$500,000.

Example 3. Power of distribution over fraction of trust income. The facts are the same as in *Example 2* except that S is given the right exercisable annually for S's lifetime to require distribution to herself of only 50 percent of the trust income for life. The remaining trust income is to be accumulated or distributed among S and the decedent's children in the trustee's discretion. The maximum amount that D's executor may elect to treat as qualified terminable interest property is \$250,000; i.e., the estate tax value of the trust (\$500,000) multiplied by the percentage of the trust in which S has a qualifying income interest for life (50 percent). If D's executor elects to treat only 20 percent of the portion of the trust in which S has a qualifying income interest as qualified terminable interest property, the deductible interest is \$50,000, i.e., 20 percent of \$250,000.

Example 4. Power to distribute trust corpus to other beneficiaries. D's will established a trust providing that S is entitled to receive at least annually all the trust income. The trustee is given the power to use annually during S's lifetime \$5,000 from the trust for the maintenance and support of S's minor child, C. Any such distribution does not necessarily relieve S of S's obligation to support and maintain C. S does not have a qualifying income interest for life in any portion of the trust because the bequest fails to satisfy the condition that no person have a power, other than a power the exercise of which takes effect only at or after S's death, to appoint any part of the property to any person other than S. The trust would also be nondeductible under section 2056(b)(7) if S, rather than the trustee, held the power to appoint a portion of the principal to C. However, in the latter case, if S made a qualified disclaimer (within the meaning of section 2518) of the

power to appoint to C, the trust could qualify for the marital deduction pursuant to section 2056(b)(7), assuming that the power is personal to S and S's disclaimer terminates the power. Similarly, in either case, if C made a qualified disclaimer of C's right to receive distributions from the trust, the trust would qualify under section 2056(b)(7), assuming that C's disclaimer effectively negates the trustee's power under local law.

Example 5. Spouse's income interest terminable on remarriage. D's will established a trust providing that all of the trust income is payable at least annually to S for S's lifetime, provided that, if S remarries, S's interest in the trust will pass to X. The trust is not deductible under section 2056(b)(7). S's income interest is not a *qualifying income interest for life* because it is not for life but, rather, is terminable upon S's remarriage.

Example 6. Spouse's qualifying income interest for life contingent on executor's election. D's will established a trust providing that S is entitled to receive the income, payable at least annually, from that portion of the trust that the executor elects to treat as qualified terminable interest property. The portion of the trust which the executor does not elect to treat as qualified terminable interest property passes as of D's date of death to a trust for the benefit of C, D's child. Under these facts, the executor is not considered to have a power to appoint any part of the trust property to any person other than S during S's life.

Example 7. Formula partial election. D's will established a trust funded with the residue of D's estate. Trust income is to be paid annually to S for life, and the principal is to be distributed to D's children upon S's death. S has the power to require that all the trust property be made productive. There is no power to distribute trust property during S's lifetime to any person other than S. D's executor elects to deduct a fractional share of the residuary estate under section 2056(b)(7). The election specifies that the numerator of the fraction is the amount of deduction necessary to reduce the Federal estate tax to zero (taking into account final estate tax values) and the denominator of the fraction is the final estate tax value of the residuary estate (taking into account any specific bequests or liabilities of the estate paid out of the residuary estate). The formula election is of a fractional share. The value of the share qualifies for the marital deduction even though the executor's determinations to claim administration expenses as estate or income tax deductions and the final estate tax values will affect the size of the fractional share.

Example 8. Formula partial election. The facts are the same as in *Example 7* except that, rather than defining a fraction, the executor's formula states: "I elect to treat as qualified terminable interest property that

portion of the residuary trust, up to 100 percent, necessary to reduce the Federal estate tax to zero, after taking into account the available unified credit, final estate tax values and any liabilities and specific bequests paid from the residuary estate." The formula election is of a fractional share. The share is equivalent to the fractional share determined in *Example 7*.

Example 9. Severance of QTIP trust. D's will established a trust funded with the residue of D's estate. Trust income is to be paid annually to S for life, and the principal is to be distributed to D's children upon S's death. S has the power to require that all of the trust property be made productive. There is no power to distribute trust property during S's lifetime to any person other than S. D's will authorizes the executor to make the election under section 2056(b)(7) only with respect to the minimum amount of property necessary to reduce estate taxes on D's estate to zero, authorizes the executor to divide the residuary estate into two separate trusts to reflect the election, and authorizes the executor to charge any payment of principal to S to the qualified terminable interest trust. S is the sole beneficiary of both trusts during S's lifetime. The authorizations in the will do not adversely affect the allowance of the marital deduction. Only the property remaining in the marital deduction trust, after payment of principal to S, is subject to inclusion in S's gross estate under section 2044 or subject to gift tax under section 2519.

Example 10. Payments to spouse from individual retirement account. S is the life beneficiary of sixteen remaining annual installments payable from D's individual retirement account. The terms of the account provide for the payment of the account balance in nineteen annual installments that commenced when D reached age 70½. Each installment is equal to all the income earned on the remaining principal in the account plus a share of the remaining principal equal to 1/19 in the first year, 1/18 in the second year, 1/17 in the third year, etc. Under the terms of the account, S has no right to withdraw any other amounts from the account. Any payments remaining after S's death pass to D's children. S's interest in the account qualifies as a qualifying income interest for life under section 2056(b)(7)(B)(ii), without regard to the provisions of section 2056(b)(7)(C).

Example 11. Spouse's interest in trust in the form of an annuity. D died prior to October 24, 1992. D's will established a trust funded with income producing property valued at \$500,000 for estate tax purposes. The trustee is required by the trust instrument to pay \$20,000 a year to S for life. Trust income in excess of the annuity amount is to be accumulated in the trust and may not be distributed during S's lifetime. S's lifetime annuity interest is treated as a qualifying income interest for life. If the executor elects to treat the entire

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portion of the trust in which S has a qualifying income interest as qualified terminable interest property, the value of the deductible interest is (assuming that 10 percent is the applicable interest rate under section 7520 for valuing annuities on the appropriate valuation date) \$200,000, because that amount would yield an income to S of \$20,000 a year.

Example 12. Value of spouse's annuity exceeds value of trust corpus. The facts are the same as in *Example 11* except that the trustee is required to pay S \$70,000 a year for life. If the executor elects to treat the entire portion of the trust in which S has a qualifying income interest as qualified terminable interest property, the value of the deductible interest is \$500,000, which is the lesser of the entire value of the property (\$500,000), or the amount of property that (assuming a 10 percent interest rate) would yield an income to S of \$70,000 a year (\$700,000).

Example 13. Pooled income fund. D's will provides for a bequest of \$200,000 to a pooled income fund described in section 642(c)(5), designating S as the income beneficiary for life. If D's executor elects to treat the entire \$200,000 as qualified terminable interest property, the deductible interest is \$200,000.

Example 14. Funding severed QTIP trusts. D's will established a trust satisfying the requirements of section 2056(b)(7). Pursuant to the authority in D's will and § 20.2056(b)–7(b)(2)(ii), D's executor indicates on the Federal estate tax return that an election under section 2056(b)(7) is being made with respect to 50 percent of the trust, and that the trust will subsequently be divided to reflect the partial election on the basis of the fair market value of the property at the time of the division. D's executor funds the trust at the end of the period of estate administration. At that time, the property available to fund the trusts consists of 100 shares of X Corporation stock with a current value of \$400,000 and 200 shares of Y Corporation stock with a current value of \$400,000. D may fund each trust with the stock of either or both corporations, in any combination, provided that the aggregate value of the stock allocated to each trust is \$400,000.

[T.D. 8522, 59 FR 9651, Mar. 1, 1994, as amended by T.D. 8779, 63 FR 44393, Aug. 19, 1998; T.D. 9102, 69 FR 21, Jan. 2, 2004]

§ 20.2056(b)–8 Special rule for charitable remainder trusts.

(a) *In general*—(1) *Surviving spouse only noncharitable beneficiary.* With respect to estates of decedents dying after December 31, 1981, subject to section 2056(d), if the surviving spouse of the decedent is the only noncharitable beneficiary of a charitable remainder annuity trust or a charitable remain-

der unitrust described in section 664 (qualified charitable remainder trust), section 2056(b)(1) does not apply to the interest in the trust that is transferred to the surviving spouse. Thus, the value of the annuity or unitrust interest passing to the spouse qualifies for a marital deduction under section 2056(b)(8) and the value of the remainder interest qualifies for a charitable deduction under section 2055. If an interest in property qualifies for a marital deduction under section 2056(b)(8), no election may be made with respect to the property under section 2056(b)(7). For purposes of this section, the term *non-charitable beneficiary* means any beneficiary of the qualified charitable remainder trust other than an organization described in section 170(c).

(2) *Interest for life or term of years.* The surviving spouse's interest need not be an interest for life to qualify for a marital deduction under section 2056(b)(8). However, for purposes of section 664, an annuity or unitrust interest payable to the spouse for a term of years cannot be payable for a term that exceeds 20 years.

(3) *Payment of state death taxes.* A deduction is allowed under section 2056(b)(8) even if the transfer to the surviving spouse is conditioned on the spouse's payment of state death taxes, if any, attributable to the qualified charitable remainder trust. See § 20.2056(b)–4(c) for the effect of such a condition on the amount of the deduction allowable.

(b) *Charitable remainder trusts where the surviving spouse is not the only non-charitable beneficiary.* In the case of a charitable remainder trust where the decedent's spouse is not the only non-charitable beneficiary (for example, where the noncharitable interest is payable to the decedent's spouse for life and then to another individual for life), the qualification of the interest as qualified terminable interest property is determined solely under section 2056(b)(7) and not under section 2056(b)(8). Accordingly, if the decedent died on or before October 24, 1992, or the trust otherwise comes within the purview of the transitional rules contained in § 20.2056(b)–7(e)(5), the spousal